

washed coal is sold and royalties are reported and paid.

[54 FR 1523, Jan. 13, 1989, as amended at 61 FR 5480, Feb. 12, 1996; 64 FR 43288, Aug. 10, 1999]

**§ 1206.259 Determination of washing allowances.**

(a) *Arm's-length contracts.* (1) For washing costs incurred by a lessee under an arm's-length contract, the washing allowance shall be the reasonable actual costs incurred by the lessee for washing the coal under that contract, subject to monitoring, review, audit, and possible future adjustment. The lessee shall have the burden of demonstrating that its contract is arm's-length. ONRR's prior approval is not required before a lessee may deduct costs incurred under an arm's-length contract. The lessee must claim a washing allowance by reporting it as a separate line entry on the Form ONRR-4430.

(2) In conducting reviews and audits, ONRR will examine whether the contract reflects more than the consideration actually transferred either directly or indirectly from the lessee to the washer for the washing. If the contract reflects more than the total consideration paid, then the ONRR may require that the washing allowance be determined in accordance with paragraph (b) of this section.

(3) If ONRR determines that the consideration paid pursuant to an arm's-length washing contract does not reflect the reasonable value of the washing because of misconduct by or between the contracting parties, or because the lessee otherwise has breached its duty to the lessor to market the production for the mutual benefit of the lessee and the lessor, then ONRR shall require that the washing allowance be determined in accordance with paragraph (b) of this section. When ONRR determines that the value of the washing may be unreasonable, ONRR will notify the lessee and give the lessee an opportunity to provide written information justifying the lessee's washing costs.

(4) Where the lessee's payments for washing under an arm's-length contract are not based on a dollar-per-unit basis, the lessee shall convert whatever

consideration is paid to a dollar value equivalent. Washing allowances shall be expressed as a cost per ton of coal washed.

(b) *Non-arm's-length or no contract.* (1) If a lessee has a non-arm's-length contract or has no contract, including those situations where the lessee performs washing for itself, the washing allowance will be based upon the lessee's reasonable actual costs. All washing allowances deducted under a non-arm's-length or no contract situation are subject to monitoring, review, audit, and possible future adjustment. The lessee must claim a washing allowance by reporting it as a separate line entry on the Form ONRR-4430. When necessary or appropriate, ONRR may direct a lessee to modify its estimated or actual washing allowance.

(2) The washing allowance for non-arm's-length or no contract situations shall be based upon the lessee's actual costs for washing during the reported period, including operating and maintenance expenses, overhead, and either depreciation and a return on undepreciated capital investment in accordance with paragraph (b)(2)(iv)(A) of this section, or a cost equal to the depreciable investment in the wash plant multiplied by the rate of return in accordance with paragraph (b)(2)(iv)(B) of this section. Allowable capital costs are generally those for depreciable fixed assets (including costs of delivery and installation of capital equipment) which are an integral part of the wash plant.

(i) Allowable operating expenses include: Operations supervision and engineering; operations labor; fuel; utilities; materials; ad valorem property taxes, rent; supplies; and any other directly allocable and attributable operating expense which the lessee can document.

(ii) Allowable maintenance expenses include: Maintenance of the wash plant; maintenance of equipment; maintenance labor; and other directly allocable and attributable maintenance expenses which the lessee can document.

(iii) Overhead attributable and allocable to the operation and maintenance of the wash plant is an allowable expense. State and Federal income

taxes and severance taxes, including royalties, are not allowable expenses.

(iv) A lessee may use either paragraph (b)(2)(iv)(A) or (B) of this section. After a lessee has elected to use either method for a wash plant, the lessee may not later elect to change to the other alternative without approval of the ONRR.

(A) To compute depreciation, the lessee may elect to use either a straight-line depreciation method based on the life of equipment or on the life of the reserves which the wash plant services, whichever is appropriate, or a unit of production method. After an election is made, the lessee may not change methods without ONRR approval. A change in ownership of a wash plant shall not alter the depreciation schedule established by the original operator/lessee for purposes of the allowance calculation. With or without a change in ownership, a wash plant shall be depreciated only once. Equipment shall not be depreciated below a reasonable salvage value.

(B) ONRR shall allow as a cost an amount equal to the allowable capital investment in the wash plant multiplied by the rate of return determined pursuant to paragraph (b)(2)(v) of this section. No allowance shall be provided for depreciation. This alternative shall apply only to plants first placed in service or acquired after March 1, 1989.

(v) The rate of return must be the industrial rate associated with Standard and Poor's BBB rating. The rate of return must be the monthly average rate as published in Standard and Poor's Bond Guide for the first month for which the allowance is applicable. The rate must be redetermined at the beginning of each subsequent calendar year.

(3) The washing allowance for coal shall be determined based on the lessee's reasonable and actual cost of washing the coal. The lessee may not take an allowance for the costs of washing lease production that is not royalty bearing.

(c) *Reporting requirements*—(1) *Arm's-length contracts.* (i) The lessee must notify ONRR of an allowance based on incurred costs by using a separate line entry on the Form ONRR-4430.

(ii) ONRR may require that a lessee submit arm's-length washing contracts and related documents. Documents shall be submitted within a reasonable time, as determined by ONRR.

(2) *Non-arm's-length or no contract.* (i) The lessee must notify ONRR of an allowance based on the incurred costs by using a separate line entry on the Form ONRR-4430.

(ii) For new washing facilities or arrangements, the lessee's initial washing deduction shall include estimates of the allowable coal washing costs for the applicable period. Cost estimates shall be based upon the most recently available operations data for the washing system or, if such data are not available, the lessee shall use estimates based upon industry data for similar washing systems.

(iii) Upon request by ONRR, the lessee shall submit all data used to prepare the allowance deduction. The data shall be provided within a reasonable period of time, as determined by ONRR.

(d) *Interest and assessments.* (1) If a lessee nets a washing allowance on the Form ONRR-4430, then the lessee shall be assessed an amount up to 10 percent of the allowance netted not to exceed \$250 per lease sales type code per sales period.

(2) If a lessee erroneously reports a washing allowance which results in an underpayment of royalties, interest shall be paid on the amount of that underpayment.

(3) Interest required to be paid by this section shall be determined in accordance with §1218.202 of this chapter.

(e) *Adjustments.* (1) If the actual coal washing allowance is less than the amount the lessee has taken on Form ONRR-4430 for each month during the allowance reporting period, the lessee shall pay additional royalties due plus interest computed under §1218.202 of this chapter from the date when the lessee took the deduction to the date the lessee repays the difference to ONRR. If the actual washing allowance is greater than the amount the lessee has taken on Form ONRR-4430 for each month during the allowance reporting period, the lessee shall be entitled to a credit without interest.

(2) The lessee must submit a corrected Form ONRR-4430 to reflect actual costs, together with any payment, in accordance with instructions provided by ONRR.

(f) *Other washing cost determinations.* The provisions of this section shall apply to determine washing costs when establishing value using a net-back valuation procedure or any other procedure that requires deduction of washing costs.

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#### § 1206.260 Allocation of washed coal.

(a) When coal is subjected to washing, the washed coal must be allocated to the leases from which it was extracted.

(b) When the net output of coal from a washing plant is derived from coal obtained from only one lease, the quantity of washed coal allocable to the lease will be based on the net output of the washing plant.

(c) When the net output of coal from a washing plant is derived from coal obtained from more than one lease, unless determined otherwise by BLM, the quantity of net output of washed coal allocable to each lease will be based on the ratio of measured quantities of coal delivered to the washing plant and washed from each lease compared to the total measured quantities of coal delivered to the washing plant and washed.

#### § 1206.261 Transportation allowances—general.

(a) For ad valorem leases subject to § 1206.257 of this subpart, where the value for royalty purposes has been determined at a point remote from the lease or mine, ONRR shall, as authorized by this section, allow a deduction in determining value for royalty purposes for the reasonable, actual costs incurred to:

(1) Transport the coal from a Federal lease to a sales point which is remote from both the lease and mine; or

(2) Transport the coal from a Federal lease to a wash plant when that plant is remote from both the lease and mine

and, if applicable, from the wash plant to a remote sales point. In-mine transportation costs shall not be included in the transportation allowance.

(b) Under no circumstances will the authorized washing allowance and the transportation allowance reduce the value for royalty purposes to zero.

(c)(1) When coal transported from a mine to a wash plant is eligible for a transportation allowance in accordance with this section, the lessee is not required to allocate transportation costs between the quantity of clean coal output and the rejected waste material. The transportation allowance shall be authorized for the total production which is transported. Transportation allowances shall be expressed as a cost per ton of cleaned coal transported.

(2) For coal that is not washed at a wash plant, the transportation allowance shall be authorized for the total production which is transported. Transportation allowances shall be expressed as a cost per ton of coal transported.

(3) Transportation costs shall only be recognized as allowances when the transported coal is sold and royalties are reported and paid.

(d) If, after a review and/or audit, ONRR determines that a lessee has improperly determined a transportation allowance authorized by this section, then the lessee shall pay any additional royalties, plus interest, determined in accordance with § 1218.202 of this chapter, or shall be entitled to a credit, without interest.

(e) Lessees shall not disproportionately allocate transportation costs to Federal leases.

[54 FR 1523, Jan. 13, 1989, as amended at 61 FR 5481, Feb. 12, 1996; 64 FR 43288, Aug. 10, 1999]

#### § 1206.262 Determination of transportation allowances.

(a) *Arm's-length contracts.* (1) For transportation costs incurred by a lessee pursuant to an arm's-length contract, the transportation allowance shall be the reasonable, actual costs incurred by the lessee for transporting the coal under that contract, subject to monitoring, review, audit, and possible future adjustment. The lessee shall have the burden of demonstrating that